Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	
Price Cap Performance Review for Local Exchange Carriers	CC Docket No. 94-1
Treatment of Operator Services Under Price Cap Regulation	CC Docket No. 93-124

NYNEX REPLY COMMENTS

The NYNEX Telephone Companies

Joseph Di Bella

1300 I Street, N.W., Suite 400 West
Washington, DC 20005
(202) 336-7894

Their Attorney

Dated: January 16, 1996

TABLE OF CONTENTS

SUMMARY

The purpose of this proceeding, which appears to have escaped some of the commenters, is to establish a framework for increasingly less stringent price regulation as competition grows for local exchange services and interstate access services. The Commission should reject the efforts of some commenters to impose additional pricing restrictions on the LECs that would impede their ability to respond to competition.

The commenters raise numerous concerns about how the Commission's regulatory policies should evolve as competition increases. In its initial comments, NYNEX proposed an Adaptive Regulatory Model that would meet the industry's concerns by providing a framework for addressing issues concerning pricing flexibility, access rate structure reform, removal of barriers to entry, and changes to the price cap system at each stage in the evolution to a fully competitive market for local exchange and interstate access services. The NYNEX model would provide a road map that would aid the industry in making decisions about network development and capital investment. The Commission should adopt such a model at this time to give the industry certainty about the regulatory environment that it will face in the future.

The Commission should make it easier, not harder, for the local exchange carriers ("LECs") to introduce new services, both as a baseline reform and as competition increases. The objections to the Commission's proposal for reduced tariff requirements for "Track 2" new services are exaggerated. The

Commission's proposal would make relatively minor modifications in the current tariff requirements. The Commission should also adopt its proposal to reduce the notice period for restructure tariffs.

The Commission should either streamline or eliminate the Part 69 waiver requirement for new switched access services as a baseline reform. USTA is correct that there is no need for the Commission to require the LECs to make a public interest showing prior to filing a tariff proposing a new switched access service. The Commission can deal with issues concerning new switched access services during the process of tariff review. If the Commission retains the waiver requirement, it should adopt time limits for acting on waiver requests, as proposed by Time Warner and Sprint.

The Commission should allow the LECs to introduce alternative pricing plans for switched access services once barriers to entry in the local exchange market have been removed. NYNEX agrees with GSA and the other LECs that APPs would produce significant public benefits.

The Commission should allow the LECs to offer individual case basis tariffs and contract tariffs when markets are open to competition, and prior to streamlined regulation. As noted by GSA, such pricing would allow the LECs to address individual customer needs and to respond to competition in competitive bidding situations.

The Commission should reject proposals to limit both downward and upward pricing flexibility in the LEC price cap system. To the contrary, such flexibility should be increased as competition increases. While several commenters express a concern about predatory pricing, such pricing becomes increasingly impractical as markets become open to competition.

The Commission should allow the LECs to consolidate price cap baskets and service categories as competition increases. It should reject proposals from commenters, such as AT&T, that would actually make the price cap system more complex by adding additional sub-categories.

Finally, the Commission should allow the LECs to place operator services and call completion services within the existing information services category. The proposals of some commenters to create new service categories for these services are additional examples of efforts to increase the complexity of the price cap system and to reduce the pricing flexibility of the LECs. This is directly the opposite of how the Commission should reform the price cap system as markets become more competitive.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	
Price Cap Performance Review for Local Exchange Carriers	CC Docket No. 94-1
Treatment of Operator Services Under Price Cap Regulation	CC Docket No. 93-124

NYNEX REPLY COMMENTS

The NYNEX Telephone Companies[1] ("NYNEX") hereby file their reply to the comments that were filed in response to the Commission's *Second Further Notice* in the above-referenced proceedings.[2]

I. Introduction

The comments in this proceeding demonstrate a wide variety of concerns about how the Commission's policies will affect the telecommunications industry and users of interstate access services. The local exchange carriers ("LECs") are concerned about their ability to move to market-based prices as competitors enter their markets. LEC competitors are concerned that the LECs would use

[1] The NYNEX Telephone Companies are New York Telephone Company and New England Telephone and Telegraph Company.

[2] Second Further Notice of Proposed Rulemaking in CC Docket No. 94-1, Further Notice of Proposed Rulemaking in CC Docket No. 93-124, FCC 95-393, released September 20, 1995 ("*Second Further Notice*").

additional pricing flexibility to offer predatory prices. LEC competitors and interexchange carriers ("IXCs") are concerned that the LECs would gain pricing flexibility before the LECs took actions to remove barriers to entry. Small IXCs are concerned that the LECs would use pricing flexibility to give greater discounts to large IXCs.

To address these concerns, the Commission should develop a regulatory framework that will match LEC pricing flexibility to the level of competition in the local exchange and interstate access markets. The industry needs to understand how the Commission's regulatory policies will evolve as competition develops so that it can make efficient decisions about network development and capital investment. Certainty about the regulatory environment will allow both suppliers and customers of access services to respond effectively to changes in the market environment.[3]

The NYNEX Adaptive Regulatory Model provides a framework that would ensure that the Commission's regulatory policies kept pace with marketplace changes. It would meet the concerns of several commenters that the Commission needs to look at competitive developments in both interstate and intrastate jurisdictions in determining when to allow additional pricing flexibility in the interstate access market.[4] The NYNEX model not only addresses pricing flexibility, but it also provides a framework for making

---

[3] *See* Sprint at p. 5; USTA at pp. 7-8; GTE at pp. 77-78; Time Warner at p. 8..

[4] *See, e.g.*, Time Warner at p. 40; LDDS at p. 4; TCG at p. 5; Comcast at p. 15.

changes in the access rate structure, in the price cap basket structure, and in the price cap productivity factors as the competitive landscape changes. This holistic approach would address concerns raised about the need to reform the access charge structure to facilitate the development of competition.

The three regulatory frameworks within Phase I of NYNEX's model would match the regulatory environment to the early stages in the introduction of local exchange competition. Phase II, streamlined regulation, and Phase III, nondominant regulation, would remove regulatory controls that would no longer be required when markets are subject to effective competition. This model would provide the industry clear notice of how the regulatory environment would evolve as competition increases.

For these reasons, the Commission should adopt the NYNEX model as a reasonable framework for dealing with the concerns raised in this proceeding. In the following sections, NYNEX responds to arguments about specific issues raised in the *Second Further Notice.*

II. The Purpose Of This Proceeding Is Not To Make The Price Cap System More Restrictive.

Several commenters entirely miss the point of this rulemaking proceeding. The Commission clearly stated that its purpose is to "consider and propose specific changes to interstate access price regulation to respond to changes in the market for these services and to rely more heavily on market

forces to achieve our public policy goals."[5] This was based on the Commission's finding that "[price cap] constraints tend to become unnecessary or counterproductive as market forces become operational."[6] Nonetheless, some commenters argue that the Commission should impose even greater regulatory restrictions on the LECs as competition emerges in the local exchange and interstate access markets. For example, they ask the Commission to:

- require the LECs to reduce their access charges to their direct costs;[7] and to recover their overhead costs only from their "retail" customers;[8]
- require the LECs to apply averaged prices throughout geographic areas where they have "shared costs;"[9]
- prohibit volume discounts and require cost support for term discounts;[10]
- require greater cost support, and impose additional standards, for Part 69 waivers;[11]
- require the LECs to maintain uniform overhead loadings on all of their access charges;[12]
- require the LECs to submit cost support for rate restructures; and[13]
- treat Alternative Pricing Plans ("APPs") as out-of-band filings.[14]

---

[5] *Second Further Notice* at para. 1.

[6] *Second Further Notice* at para. 21.

[7] *See* MCI at p. 11; CompTel at p. 19. MCI also wants the Commission to require the LECs to make exogenous cost reductions for the extent to which the rates for new services exceed direct costs. This proposal is completely inconsistent with price cap regulation. Indeed, MCI is quite candid in admitting that its proposals would require the Commission to abandon price cap principles and to revert to rate-of-return regulation. *See* MCI at p. 11.

[8] *See* CompTel at p. 19.

[9] *See* Time Warner at p. 44.

[10] *See* CompTel at p. 20.

[11] *See, e.g.*, CompTel at p. 31; MCI at pp. 12, 17.

[12] *See* CompTel at p. 22.

[13] *See* Ad Hoc at p. 11.

[14] *See* Ad Hoc at p. 14.

These proposals would substantially reduce the amount of pricing flexibility that the LECs have under the current price cap rules, which were designed to enhance economic efficiency even in a monopoly environment. They are completely inappropriate in a competitive environment, where market forces would be far more effective than government regulation in promoting economic rates.

The purpose of this proceeding, which appears to have escaped some of the commenters, is to establish a framework for reducing the level of price regulation as competition grows for local exchange services and interstate access services. The Commission should reject the efforts of some commenters to impose pricing restrictions on the LECs that would impede their ability to respond to competition.

III. The Commission Should Develop An Adaptive Regulatory Model That Would Match The Regulatory Environment To The Level Of Competition.

Several commenters argue that the Commission should not even consider granting the LECs additional pricing flexibility until it has taken action on other issues such as universal service, access charge reform, and interconnection.[15] They also argue that it is too early to establish standards for granting

[15] *See, e.g.*, AT&T at pp. 5-6; Sprint at p. 5; Teleport at p. 5; LDDS at p. 2.

streamlined regulation or for determining when a LEC is nondominant in a particular service and/or geographic area.[16]

These arguments are not well-founded. A proceeding to develop a framework for pricing flexibility is not incompatible with access charge reform or with consideration of universal service and interconnection. Quite to the contrary. As Chairman Hundt recently stated, the Commission needs to deal with all of these issues contemporaneously in order to promote the transition to local exchange competition.[17] The Chairman noted that the level and structure of access charges are not economic, and that uneconomic rates inhibit the development of a competitive market. Uneconomic rates send incorrect pricing signals to the market, cause inefficient investment decisions, and often drive customers to the less efficient carrier. The Commission needs to address these issues now to give both new entrants and customers a clear vision of how access regulation will adapt to increasing levels of competition.[18]

---

[16] *See, e.g.,* MCI at p. 33; Ad Hoc at p. 30; Sprint at p. 25.

[17] *See* speech by Chairman Reed Hundt at December 5, 1995 Telecommunications Reports seminar on interconnection.

[18] Sprint and TCG claim that there is minimal competition in the interstate access market. They argue that, in LATA 132, where Sprint selected TCG to provide all of its local transport services for Sprint's switched access services in the New York LATA, NYNEX still continues to receive at least 96% of Sprint's payments for Switched Access services. *See* Sprint at p. 25; TCG at pp. 2-4. TCG also states that it pays 71% of its local switched service revenues to NYNEX.

The statistics quoted by both TCG and Sprint are very misleading. TCG admits that it only provides Sprint with local transport services, while the 96% figure is a measure of total access revenue, including revenues from transport services, carrier common line charges, local switching charges, and interconnection charges. In addition, percentages of access revenues are not good measures of market share, since TCG may charge significantly less than

In its initial comments, NYNEX proposed an "Adaptive Regulatory Model" that would allow the Commission to "rely more heavily on market forces to achieve [the Commission's] policy goals."[19] This model would provide a framework for coordinating the Commission's policies on pricing flexibility with actions in other proceedings, such as access charge reform, interconnection, and price cap reform.[20] The comments in this proceeding demonstrate the virtue of such a model; it would ensure that the concerns of all parties were addressed at the appropriate time in the transition to competition.

One of the most important features of the NYNEX model is the proposal to create a "Phase I-B" level of pricing flexibility that would be triggered by the elimination of barriers to entry in a substantial portion of a LEC's service area and by the presence of at least one local exchange competitor.[21] This would provide an incentive for the LECs to take affirmative actions to eliminate barriers to entry.

Some parties maintain that, instead of providing incentives for the price cap LECs to remove barriers to entry, the Commission should penalize LECs for

---

NYNEX for transport services. A more accurate comparison would be by percentage of demand. NYNEX estimates it only retains 50% of the High Capacity market in New York measured by DS1 equivalent circuits. Both Sprint and TCG acknowledge that TCG provides the majority of Sprint's local transport service in LATA 132. NYNEX is also aware that another major IXC has moved 58% of its switched transport services to competing access providers in Manhattan. This shows that competitors have captured a significant share of the access markets that they have chosen to serve in New York.

[19] *Second Further Notice* at para. 1.

[20] *See* NYNEX at pp. 10-12 & Attachment A.

[21] *See* NYNEX at pp. 20-22.

failing to remove such barriers.[22] This would be short-sighted. While the Commission has both the power and the responsibility to enforce its interconnection standards on all carriers, there are many areas where LECs can take steps above and beyond the letter of the law to promote competition. For instance, NYNEX offers physical collocation despite the absence of any legal requirement to do so, and it has entered into interconnection and mutual compensation agreements with several competitive local exchange carriers ("CLECs") pursuant to policies of state regulatory commissions that encouraged inter-carrier agreements.[23] The Commission should adopt policies that would encourage cooperation between carriers, rather than litigation. The NYNEX proposal would provide such encouragement by linking pricing flexibility to efforts by the LECs to remove barriers to competition.

Many of NYNEX's proposals with regard to the application of streamlined regulation in Phase II were supported by other commenters, such as the NYNEX proposal that density-based zones should not be used as the relevant geographic market.[24] The commenters also supported NYNEX's proposal to use groupings of contiguous wire centers as the relevant market[25] and to use specific services as the relevant services. Several commenters

---

[22] *See, e.g.*, Time Warner at p. 32.

[23] In these reply comments, NYNEX refers to LEC competitors collectively as "CLECs," which includes competitive local exchange carriers, competitive access providers, cable companies, interexchange carriers, and any other carriers that offer services that compete with LEC services.

[24] *See, e.g.*, MCI at p. 31; Time Warner at p. 49; AT&T at p. 13; Ad Hoc at p. 30.

[25] *See, e.g.*, TRA at p. 18.

supported NYNEX's proposal to require a showing that barriers to entry have been removed and that competitors have established some level of market coverage as prerequisites for lessened regulation and increased pricing flexibility in Phases I-B and I-C.[26] Several commenters also agreed that the Commission should require a level of market penetration by competitors for Phase II, streamlined regulation.[27]

IV. The Commission Should Make It Easier For The LECs To Introduce New Services.

A. The Tariff Review Process For New And Restructured Services Should Be Streamlined As A Baseline Reform.

The *Second Further Notice* proposes to encourage the introduction of new services by shortening the notice periods and by reducing the cost support for certain types of new services categorized as "Track 2."[28] Some commenters oppose this proposal, arguing that the current rules are needed to detect predatory pricing against competitors[29] or discriminatory pricing against customers.[30] Ad Hoc, Time Warner, and NCTA support a reduced level of regulation based on whether the services are competitive,[31] while GSA maintains that more flexible rules

---

[26] *See, e.g.*, AT&T at p. 21; Sprint at p. 27; Time Warner at p. 23; NCTA at p. 11; MFS at p. 7; TRA at pp. 20-21.

[27] *See, e.g.*, AT&T at p. 17; MCI at p. 34; TRA at p. 31; NCTA at p. 11.

[28] *See Second Further Notice* at para. 49.

[29] *See, e.g.*, MFS at pp. 2-4; California Cable TV Assoc. at pp. 22-25; Sprint Telecommunications Venture at pp. 6-10; LDDS at pp. 29-31.

[30] *See, e.g.*, AT&T at pp. 23-26; CompTel at pp. 26-27.

[31] *See* Ad Hoc at p. 48; Time Warner at pp. 10-13; NCTA at pp. 22-23.

should be adopted regardless of the competitiveness of the new service.[32] Sprint proposes making no distinction by Track, but rather reducing the notice period for all new services to 30 days.[33]

NYNEX supports the Commission's proposal to reduce the notice period and the level of cost support for Track 2 services as a "baseline" reform. The timely introduction of new services is in the public interest regardless of the degree of competition for those services.

Some commenters have exaggerated the effects that the Commission's proposal would have on competitors and customers.[34] The Commission's proposal would not radically depart from the current tariff requirements. It would merely reduce unnecessary requirements, and it would make it easier for the LECs to introduce new services that would be responsive to customer demand. The 14-day comment period and the requirement that the LECs submit direct cost support would provide the Commission and interested parties an adequate opportunity to review a tariff proposing a new Track 2 service, while

---

[32] *See* GSA at p. 4.

[33] *See* Sprint at pp. 14-15.

[34] MFS argues that the LECs could "manipulate" the service definitions and reclassify an existing service as "new" to evade regulatory scrutiny. *See* MFS at p. 2. As an example of such manipulation, MFS cites NYNEX Enterprise service, which NYNEX proposed as a new service, but which MFS considers directly substitutable for tariffed private line services in many applications. However, by filing Enterprise as a new service, NYNEX subjected itself to much greater tariff review than if it had simply filed a rate reduction for existing services. Even under Track 2 treatment, a tariff filing for a new service would involve greater cost support and tariff review than a tariff designed to reprice existing services within the band limits.

meeting the Commission's objective of eliminating unreasonable restrictions and undue delays.

Since the Commission proposes to exclude alternative pricing plans ("APPs") from the definition of new services, the streamlined review for Track 2 services would be targeted to "truly" new services rather than to discounted versions of existing services. Thus, it would exclude the types of new services that raise the greatest concern among customers with regard to discriminatory treatment.

Some commenters were concerned that drawing any distinctions between Track 1 and Track 2 services might cause definitional debates.[35] The Commission could minimize such debates by adopting a clear definition that would classify Track 1 services as those that the Commission requires the LECs to offer (*e.g.*, collocation) and those that the Commission specifically decides to place under heightened scrutiny. All other new services would be subject to Track 2 treatment. Such a definition would be easy for the carriers to understand and for the Commission to administer.

The *Second Further Notice* also proposes to reduce the notice period for restructures from the current 45 day requirement.[36] The same parties that oppose any changes to the rules for new services also oppose changes to the rules for restructures, arguing there is no need to do so and/or that there is

---

[35] *See, e.g.*, Ad Hoc at p. 6; Sprint at p. 14; Cincinnati Bell at pp. 5-6.

[36] *See Second Further Notice* at para. 51.

insufficient competition to warrant any rule change.[37] However, the Commission's experience under price caps shows that there is no need for a 45 day review period for rate restructures. The Commission's current rules do not require the LECs to submit cost support for rate restructures, and the LECs need only show that the restructured rates remain within price cap index limits and service band limits. The Commission can review such information in far less than 45 days. A shorter notice period would still allow interested parties to raise any issues concerning unreasonable rate levels or discriminatory pricing, while enhancing the ability of the LECs to restructure their rates in response to competition.

B. The Part 69 Waiver Process Should Be Streamlined Or Eliminated As A Baseline Reform.

The Commission proposes to relax the requirements for waivers of the Part 69 rules to encourage the introduction of new Switched Access services in a more expeditious manner.[38] Several commenters oppose any relaxation of the waiver standard, and some want the Commission to require more data with a waiver request, and to make the waiver standard more stringent.[39] Three commenters - AT&T, LDDS, and NCTA -- are steadfast in opposing any changes prior to access reform, as they believe that any changes now may render the current

---

[37] *See, e.g.*, AT&T at p. 26; Time Warner at p. 15; CompTel at p. 27; Ad Hoc at pp. 9-12.

[38] *See Second Further Notice* at para. 66.

[39] *See, e.g.*, MCI at pp. 12, 17.

Part 69 rate structure restrictions useless before the Commission has entertained serious debate on the issue.[40] CompTel, Ad Hoc, and TRA would support changing the waiver requirement to a public interest showing, but each wants specific, different, and somewhat detailed information as part of a showing.[41] They are also concerned about the time period allowed for comments on "me-too" petitions. GSA supports the Commission's proposal as is.[42] Rather than change the basis of the waiver requirements, Time Warner and Sprint recognize that one of the biggest problems with the waiver request process is that it has no time limit for rulings.[43] To that end, Time Warner proposes a requirement that the Commission act on waiver requests within 120 days; Sprint proposes a time limit of 90 days.[44] Time Warner does not want the underlying Part 69 rules called into question, but proposes to exempt new services based on new technologies (because rate structures for these are not currently prescribed). USTA proposes that all new services be presumed to be in the public interest without a showing.[45]

USTA is correct that there is no need for the Commission to require the LECs to make a public interest showing prior to filing rates for new Switched Access services. Such a showing has never been required for Special Access

---

[40] *See* AT&T at pp. 33-38; LDDS at p. 32; NCTA at p. 27.
[41] *See* CompTel at p. 31; Ad Hoc at pp. 16-17; TRA at pp. 29-30.
[42] *See* GSA at pp. 4-5.
[43] *See* Time Warner at pp. 18-19; Sprint at p. 20.
[44] *See id.*
[45] *See* USTA at p. 20.

services, which are effective substitutes for Switched Access services for large business customers.

Switched Access APPs, which would be excluded from the definition of "new" services under the Commission's proposal, would continue to be subject to the Part 69 waiver requirement. However, if the Commission adopts NYNEX's proposal to allow APPs in Phase I-B, when barriers to entry have been removed and when at least one competitor has begun operating, there would be no need to retain the additional requirement that a LEC obtain a Part 69 waiver prior to filing an APP tariff. Therefore, APPs, like new services, should not require Part 69 waivers.

If the Commission decides not to eliminate the Part 69 waiver requirement, it should adopt a reasonable time limit for action on waiver requests, as proposed by Time Warner and Sprint. This would do a great deal to facilitate the introduction of new Switched Access services by the LECs, and it would help them respond on a timely basis to competitive offerings.

V. Alternative Pricing Plans Should Be Allowed When Barriers To Entry Have Been Removed.

Several commenters oppose the Commission's proposal to allow the LECs to introduce APPs in addition to the volume and term discounts currently allowed. Some of the IXCs are concerned that LECs will devise APPs that will discriminate among different-sized IXCs or in favor of a LECs' long distance

affiliate if the former Bell Operating Companies are allowed to enter the long distance market.[46] LEC competitors are concerned that LECs will devise APPs that will somehow foreclose or impede competition.[47] On the other hand, GSA and the LECs note the significant consumer benefits of APPs.[48] Two commenters -- AT&T and CompTel -- specifically oppose volume discounts for switched access services beyond those currently allowed for local transport, arguing that there is no cost basis for such discounts, and that such discounts would have differential impacts on the IXCs. AT&T would specifically prohibit discounts for subsidy rate elements such as the IC and the CCL charge.

NYNEX continues to believe that the LECs should be allowed to offer APPs once barriers to entry have been removed (Phase I-B in the NYNEX Adaptive Regulatory Model). As the Commission recognized during the debate over the restructure of switched transport rates, differential impacts on IXCs cannot be controlled by prohibiting the LECs from offering discounts once competitors are in a position to offer such discounts. If the Commission prohibited APPs, it would harm the LECs, who would be prevented from responding to competition, and it would harm LEC customers, who would otherwise benefit from APPs.

---

[46] *See, e.g.*, CompTel at pp. 27-29; AT&T at pp. 28-29; MCI at p. 12; Sprint at pp. 16-17.

[47] *See, e.g.*, STV at p. 8; Time Warner at pp. 15-16; NCTA at pp. 24-25; MFS at p. 5.

[48] *See, e.g.*, GSA at p. 5; USTA at pp. 22-25.

Although NYNEX believes that APPs would be in the public interest regardless of the degree of competition, there is no reason to prohibit APPs once competitors are present. The LECs should not be prohibited from offering APPs until competition is so far advanced as to warrant streamlined regulation. AT&T was permitted to offer APPs prior to streamlined regulation, and even before one of the main barriers to entry in the long distance market -- the lack of equal access -- was removed.

Unlike new services, APPs should be incorporated into price caps immediately. To the extent that APPs represent real price reductions, the LECs should be given credit for these reductions in the price cap indexes. Of course, promotional offerings (less than 90 days) should also be allowed, but, as proposed by the Commission, they would not be incorporated into the price cap indexes.

While there may be some disagreement about whether subsidy rate elements, such as the CCL and IC charges, should be included in APPs, this should not impede the expedited offering of APPs for other rates and services. Under NYNEX's adaptive model, the subsidy rate elements would be subject to restructure or alternate recovery methods at the appropriate phase, based upon a competitive showing and a different review process.

VI. Individualized Tariffs Should Be Permitted When Barriers To Entry Have Been Removed And Competitors Have Established A Market Presence.

In the *Second Further Notice*, the Commission proposed to codify its current policies on individual case basis ("ICB") tariffs and to allow contract tariffs only after a service is subject to substantial competition and streamlined regulation.[49] Not surprisingly, LEC competitors, who are well aware of how these proposals would impede the LECs' ability to respond to competitive bids, support these proposals.[50] The IXCs, who are also potential LEC competitors, also support the proposals, and they offer unfounded arguments based on the potential for discrimination and cross-subsidization.[51] AT&T, despite its own history of court battles to employ contract pricing for its services through Tariff 12 and Tariff 15 offerings, prior to streamlined regulation, now advises that the proposed restrictions on ICB pricing by the LECs should be "strictly enforced." [52]

The approach toward ICB and contract pricing in the *Second Further Notice* is inconsistent with the guidelines that the Commission established for this rulemaking.[53] The extremely limited circumstances under which the Commission would allow ICB pricing, combined with the prohibition of contract pricing prior to streamlined regulation, would impede the development of real competition, market-based pricing, efficiency and consumer benefits. It would

---

[49] *See Second Further Notice* at paras. 65, 148.
[50] *See, e.g.*, MFS at pp. 6-8; NCTA at p. 25; Time Warner at pp. 16 & 60.
[51] *See, e.g.*, MCI at pp. 14 & 34; Sprint at p. 18; CompTel at pp. 30 & 40.
[52] *See* AT&T at p. 32.
[53] *See Second Further Notice* at para. 29.

not permit the LECs to respond to the efforts of LEC competitors to meet the specialized needs of individual customers and to offer market-based arrangement-specific rates to large customers.

GSA recognizes that the Commission's restrictive approach to ICB pricing would not allow, or at least would not facilitate, LEC offerings of specialized arrangements that would meet the unique needs of large end users. [54] GSA also recognizes that if the LECs could not offer contract pricing prior to streamlined regulation, they would not be able to respond to many customer requests for single, integrated service packages with market-based prices that would benefit end users.

NYNEX agrees with GSA's analysis. Contract pricing and individualized tariffs by the LECs should be conditioned upon "the competitiveness shown for the contracts, not for the constituent services within the contracts."[55] This would be consistent with NYNEX's proposal to allow the LECs to respond with contract tariffs to requests for proposals ("RFPs") in Phase I-C, prior to streamlined regulation, when barriers to entry have been removed and when competitors are present in most of a LEC's service area. This would ensure that individualized pricing would only be allowed when a competitor was also in a position to respond to an RFP.

---

[54] *See* GSA at pp. 8-11, 14-16.

[55] GSA at p. 16.

The GSA and NYNEX proposals would benefit customers by allowing the LECs to address individual customer needs and by stimulating true competition, thereby expanding customer choices, improving service options, and promoting lower prices. The fears of some commenters regarding potential discrimination and anticompetitive pricing are unfounded, as the contract arrangements would be made generally available to similarly-situated customers, and as the contract terms would be made public. Rates for other tariffed services would not be affected, as the contract rates and revenues would be kept outside of price caps as they were for AT&T's Tariff 12 offerings. For these reasons, it would be in the public interest for the Commission to allow individualized pricing prior to streamlined regulation.

VII. Lower Service Band Limits Should Be Eliminated And Price Cap Baskets And Service Categories Should Be Consolidated As Competition Develops.

A. The Commission Should Adopt Its Proposals To Increase Downward Pricing Flexibility.

While many commenters support some level of additional downward pricing flexibility, some propose restrictions on how that flexibility should be granted[56] or oppose any additional downward flexibility.[57] AT&T, for example, argues that LECs should not be permitted to compensate for "below-band" price

---

[56] *See, e.g.*, Ad Hoc at p. 19; MCI at p.20.

[57] *See, e.g.*, Time Warner at p. 21; NCTA at p. 21.

reductions with price increases in other service bands.[58] AT&T proposes to exclude any price reductions beyond the existing lower limits from the basket Actual Price Index ("API") calculation.[59] AT&T also argues that upper pricing flexibility should be limited to 1% for any service category in which a LEC reduces prices below the former SBI limit.

AT&T's proposal would significantly increase the complexity of a plan that already includes the calculation of literally dozens of indices (by basket, service category, subservice category and zone). AT&T argues that these burdensome safeguards are necessary because elimination of the lower SBI limits would substantially increase the LECs' flexibility to compensate for rate decreases by raising the rates in other bands.[60] However, AT&T's analysis does nothing more than demonstrate that if the SBI upper band limit is +5%, then prices for that band may be increased up to 5% annually.[61] At the start of price cap regulation, the Commission determined that an upper pricing band of 5%

---

[58] *See* AT&T at p. 41.

[59] AT&T concedes that this proposal would require LECs to report two sets of prices for bands when they price below the former band limits, and that it would require calculating separate indices for each set of prices.

[60] *See* AT&T at p. 41 and Appendix B.

[61] AT&T's example demonstrates that if decreases for "Band 1" were limited to 10%, the amount of the increase to "Band 2" would be the "10%" dollar amount. Depending on the relative revenue weights of the service categories, a 10% dollar decrease in one category may equate to less than a 5% increase in another category. That is what AT&T's example shows. Since its Band 1 category revenue is $1000, a 10% rate decrease in that category would equate to less than a 2% increase in its Band 2 category, which has revenue of $4000. With unlimited downward flexibility, a greater decrease in Band 1 could be offset with an increase in Band 2, but to no more than the upward flexibility limit of +5% per year for Band 2.